Office-Supreme Court, U.S.
FEB 9

No. 94, Original

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

State of South Carolina,

Plaintiff,

vs.

Donald T. Regan, Secretary of the Treasury of the United States of America,

Defendant.

MOTION FOR LEAVE TO FILE COMPLAINT, COMPLAINT AND SUPPORTING BRIEF

T. TRAVIS MEDLOCK
Attorney General

C. TOLBERT GOOLSBY, JR.
Chief Deputy Attorney General

DAVID C. ECKSTROM
Assistant Attorney General

GRADY L. PATTERSON, III
Assistant Attorney General

Post Office Box 11549
Columbia, SC 29211
(803) 758-3970

SINKLER GIBBS & SIMONS
Huger Sinkler *
Karen LeCraft Henderson
Faye A. Flowers

Post Office Box 11458
Columbia, SC 29211
(803) 765-1885

ATTORNEYS for Plaintiff.

* Counsel of Record.

2012

I N D E X

	Page
Motion for Leave to File Complaint.....	1
Complaint.....	3
Exhibits to Complaint.....	11
Brief in Support of Motion.....	19

No. _____, Original

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

State of South Carolina,

Plaintiff,

vs.

Donald T. Regan, Secretary of the Treasury of the United States of America,

Defendant.

MOTION FOR LEAVE
TO FILE COMPLAINT

Pursuant to Rule 9.3 of the Rules of the Supreme Court of the United States, the plaintiff State of South Carolina respectfully asks leave of the Court to file the Complaint which is submitted herewith for the reasons stated therein and in the attached supporting brief.

T. TRAVIS MEDLOCK
Attorney General

C. TOLBERT GOOLSBY, JR.
Chief Deputy Attorney General

DAVID C. ECKSTROM
Assistant Attorney General

GRADY L. PATTERSON, III
Assistant Attorney General

Post Office Box 11549
Columbia, SC 29211
(803) 758-3970

SINKLER GIBBS & SIMONS
Huger Sinkler *
Karen LeCraft Henderson
Faye A. Flowers

Post Office Box 11458
Columbia, SC 29211
(803) 765-1885

By: Huger Sinkler
ATTORNEYS for Plaintiff.

February 2nd, 1983

*Counsel of Record.

No. _____, Original

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

State of South Carolina,

Plaintiff,

vs.

Donald T. Regan, Secretary of the Treasury of the United States of America,

Defendant.

C O M P L A I N T

The plaintiff State of South Carolina ("South Carolina") brings this action in equity against the defendant and for its cause of action states that:

1. The plaintiff is a sovereign State of the United States, is one of the thirteen founding States and is an original party to the compact of sovereign States known as the Constitution of the United States.

2. The defendant is a resident and citizen of Virginia and is the duly appointed,

qualified and acting Secretary of the Treasury of the United States.

3. The original jurisdiction of this Court is invoked under Article III, Section 2 of the Constitution of the United States.

4. As one of its essential sovereign functions and in the course of the exercise of its sovereign responsibility, South Carolina must borrow money to enable it to function effectively as a provider of services essential to the health and welfare of its citizens. By the Tenth Amendment to the Constitution of the United States, South Carolina has been guaranteed the power to borrow money when and as it chooses. Pursuant to Article X, Section 13 of the South Carolina Constitution of 1895, as amended, South Carolina is authorized to borrow money and to issue general obligation and other bonds.

5. On August 19, 1982, the Congress of the United States enacted Public Law 97-248,

the "Tax Equity and Fiscal Responsibility Act of 1982 ("the Act"), and, on September 3, 1982, the President of the United States approved the Act to become effective on January 1, 1983. Section 310(b)(1) of the Act, whose effective date of implementation was subsequently suspended until July 1, 1983, requires that obligations, including State obligations evidencing State borrowing, must be issued in fully registered form in order that interest paid thereon by South Carolina to its lenders remain exempt from federal income taxation, as is manifested by the provisions of Section 310(b)(1), a copy of which is attached hereto, made a part hereof and designated Exhibit A.

6. The defendant as Secretary of the Treasury of the United States is mandated by Title 26, Section 7801 of the United States Code to enforce the provisions of Section 310(b)(1) of the Act.

7. Section 310(b)(1) of the Act

impermissibly imposes conditions upon the power of South Carolina to borrow money for public purposes by requiring that either a State must issue bonds in fully registered form or the interest which it pays upon its borrowings will be subject to federal income taxation and thus unconstitutionally impairs the ability of South Carolina to function effectively as a sovereign in violation of the Tenth Amendment to the Constitution of the United States in that it abridges South Carolina's sovereign right to borrow money by issuing debt obligations in the form that it deems desirable.

8. As is manifested by the affidavit of the State Treasurer of South Carolina, a copy of which affidavit is attached hereto, made a part hereof and designated Exhibit B, South Carolina has throughout its history found it essential to its functions as a sovereign to borrow money, primarily through the issuance of general obligation bonds, and fully intends to continue to issue general obligation bonds after

June 30, 1983, the effective date of Section 310(b)(1) of the Act. The conditions and restrictions imposed upon its borrowing power by the provisions of Section 310(b)(1) of the Act materially infringe upon the exercise of that power, including increasing the cost thereof, as is more fully set forth in Exhibit B.

9. The Congress of the United States has no power whatsoever to impose an income tax upon the interest paid by South Carolina to its lenders. Such tax exemption does not result from the pertinent provisions of Section 103 of the Internal Revenue Code. Those provisions merely recognize the tax exemption which results from the sovereignty of the States in their relationship with the national government. The Sixteenth Amendment to the United States Constitution neither changed nor proposed to change this relationship. If the Congress may tax by direct or indirect means the interest paid by South Carolina on

its borrowings, the result will be the destruction of the federal system.

10. The application of Section 310(b)(1) of the Act to the general obligations of South Carolina causes irreparable injury to South Carolina and results in the destruction of its sovereignty for which there is no remedy at law.

WHEREFORE, the plaintiff prays:

A. That the Court grant the plaintiff's motion for leave to file its complaint and assume original jurisdiction of this cause;

B. That the Court enter a decree adjudging Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 as applied to the general obligations of South Carolina to be in violation of the Constitution of the United States;

C. That the Court enter a decree permanently enjoining and restraining the defendant

from enforcing or attempting to enforce Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 against the general obligations of South Carolina; and

D. That the Court grant such other and further relief as it may deem proper and necessary.

T. TRAVIS MEDLOCK
Attorney General

C. TOLBERT GOOLSBY, JR.
Chief Deputy Attorney General

DAVID C. ECKSTROM
Assistant Attorney General

GRADY L. PATTERSON, III
Assistant Attorney General

Post Office Box 11549
Columbia, SC 29211
(803) 758-3970

SINKLER GIBBS & SIMONS
Huger Sinkler
Karen LeCraft Henderson*
Faye A. Flowers

Post Office Box 11458
Columbia, SC 29211
(803) 765-1885

ATTORNEYS for Plaintiff.

*Counsel of Record.

February 23, 1983

STATE OF SOUTH CAROLINA)
)
COUNTY OF RICHLAND)

VERIFICATION

PERSONALLY appeared before me, GRADY L. PATTERSON, JR., who, being duly sworn, deposes and says that he is the State Treasurer of South Carolina; that he has read the foregoing Complaint and knows the contents thereof; that the same are true of his own knowledge, except as to those matters and things stated therein upon information and belief, and that as to those matters and things, he believes them to be true.

GRADY L. PATTERSON, JR.
State Treasurer of South Carolina

SWORN to and subscribed
before me this 7th day
of February, 1983.

Sandra A. Lee (L.S.)
NOTARY PUBLIC FOR SOUTH CAROLINA

My Commission expires: 12/10/90

Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 provides as follows:

> (b) OTHER OBLIGATIONS. --
>
> (1) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.-- Section 103 (relating to interest on certain governmental obligations) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:
>
> '(j) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.--
>
> '(1) IN GENERAL.-- Nothing in subsection (a) or in any other provision of law shall be construed to provide an exemption from Federal income tax for interest on any registration-required obligation unless the obligation is in registered form.
>
> '(2) REGISTRATION-REQUIRED OBLIGATION.-- The term "registration-required obligation" means any obligation other than an obligation which--
>
> '(A) is not of a type offered to the public,
>
> '(B) has a maturity (at issue) of not more than 1 year or
>
> '(C) is described in section 163(f)(2)(B).

'(3) SPECIAL RULES.--

'(A) BOOK ENTRIES PERMITTED.-- For purposes of paragraph (1), a book entry obligation shall be treated as in registered form if the right to the principal of, and stated interest on, such obligation may be transferred only through a book entry consistent with regulations prescribed by the Secretary.

'(B) NOMINEES.-- The secretary shall prescribe such regulations as may be necessary to carry out the purpose of paragraph (1) where there is a nominee or chain of nominees.' P.L. 97-248, 96 STAT. ____ (1982).

STATE OF SOUTH CAROLINA)
) AFFIDAVIT
COUNTY OF RICHLAND)

PERSONALLY appeared before me, Grady L. Patterson, Jr., who being duly sworn, stated:

1. That he is the duly elected, qualified and acting Treasurer of the State of South Carolina, an office created by the Constitution of South Carolina, and as such is responsible for and oversees the issuance of general obligation bonds by the State of South Carolina.

2. That South Carolina has issued general obligation bonds each year for several decades and plans to issue general obligation bonds subsequent to June 30, 1983. Approximately $247 million of unissued general obligation bonds have heretofore been authorized by the General Assembly of South Carolina. It is planned that these bonds will be issued over the next three years. Preparations must be made prior to issuing the bonds, including

compilation of an official statement, public advertisement, preparation of bid form, printing and official resolution of the State Budget and Control Board permitting the sale. These preliminary steps require a minimum of seven weeks with a greater amount of time normally allowed.

3. General obligation bonds evidence general obligation debt, which is debt secured in whole or in part by a pledge of the full faith, credit and taxing power of the State. The Constitution of South Carolina provides that general obligation debt may be incurred only for a public purpose.

4. Throughout its history South Carolina has found it essential to the integral operation of its government to borrow money. General obligation bonds are issued to provide and maintain essential governmental functions. For example, the proceeds from general obligation bonds have been and are planned to be used to construct prisons, schools, colleges,

highways, public buildings and port facilities. As of December 2, 1982, the principal amount of South Carolina general obligation bonds outstanding was $614.5 million.

5. According to the Daily Bond Buyer, in 1982 alone there was a total of $74.876 billion of municipal securities issued. Of that amount States issued a total of $19.3 billion according to the Public Securities Association of New York.

6. Without incurring long-term debt, South Carolina would not be able to provide the essential capital improvements nor fulfill its traditional role as provider of the prisons, schools, colleges, highways, public buildings and port facilities that are necessary to the functioning of the State and the welfare of its citizens.

7. The conditions and restrictions imposed upon South Carolina's borrowing power by the provisions of Section 310(b)(1) of Public Law 97-248, the Tax Equity and Fiscal

Responsibility Act of 1982 ("Section 310(b)(1)"), will materially interfere with and infringe upon the authority of South Carolina to borrow funds as illustrated by the examples appearing below.

8. If South Carolina were to evidence its borrowings by fully registered bonds, it would pay an estimated additional .25% interest on its borrowings. To illustrate, on November 9, 1982, South Carolina sold $115 million in State Capital Improvement General Obligation Bonds at public sale. The bonds, which mature over a period of fifteen years and two months, were offered as coupon bonds with the privilege of registration as to principal and as to both principal and interest. South Carolina received four bids, the lowest being that of a syndicate headed by Citibank, N.A., which produced an interest cost of 8.667%. The total interest to be paid by South Carolina over the life of the bonds will be Ninety-seven Million Two Hundred Forty-seven Thousand Six Hundred Sixty-eight and No/100 ($97,247,668.00) Dollars.

Had the bonds been offered as fully registered bonds, registrable as to both principal and interest, it is estimated that the interest cost would have been at least twenty-five (25) basis points higher or 8.92%. This would have added more than $2.8 million to the interest that South Carolina must pay. Of obvious significance is the fact that, despite the purchasers' being able to elect to receive fully registered bonds in whole or in part, no fully registered bonds were requested and the entire issue consisting of twenty-three thousand $5,000 pieces was delivered in coupon form without registration of any sort. Bond registrars and fees for transfer agents for bonds issued in registered form will add additional costs.

9. If South Carolina should decline to issue registered bonds and, instead, should continue to issue coupon bonds as has been its practice, Section 310(b)(1) would destroy the tax-exempt status of the interest to be paid by South Carolina to its lenders. The bond

market indicates that destruction of the tax-exempt status of the interest paid by South Carolina would force South Carolina to pay approximately 3% to 5% more by way of interest rates. In the example cited above this cost would be between $30 million and $50 million.

10. As manifested by the above example, Section 310(b)(1) materially infringes upon the essential operations of the government of South Carolina by restricting its authority to borrow money and by imposing an additional burden upon its borrowings.

FURTHER saith the deponent not.

GRADY L. PATTERSON, JR.

SWORN to and subscribed
before me this 7th day
of February, 1983.

Sandra A. Gee (L.S.)
NOTARY PUBLIC FOR SOUTH CAROLINA

My Commission Expires: 12/10/90

No. _____, Original

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

State of South Carolina,

Plaintiff,

vs.

Donald T. Regan, Secretary of the Treasury of the United States of America,

Defendant.

BRIEF IN SUPPORT OF MOTION TO FILE COMPLAINT

QUESTIONS PRESENTED

I. Do the provisions of Section 310 (b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982, which require that debt obligations issued by the plaintiff must be in registered form in order that the interest paid thereon be exempt from federal income taxation, violate the United States Constitution and the Tenth Amendment thereto by abridging the plaintiff's power to borrow money?

II. Do the provisions of Section 310

(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 violate the United States Constitution by subjecting the interest paid on the debt obligations issued by the plaintiff in bearer form to federal income taxation?

TABLE OF CONTENTS

	Page
Jurisdiction	27
Constitutional and statutory provisions involved	27
Statement	29
Summary of Argument	31
Argument	
I. The complaint manifests a justiciable controversy over which the Court has and should assume original jurisdiction	32
II. Section 310(b)(1) of the Act violates the the United States Constitution and the Tenth Amendment thereto by abridging the plaintiff's power to borrow money	44
III. Section 310(b)(1) of the Act violates the United States Constitution by subjecting the interest paid on the debt obligations issued by the plaintiff in bearer form to federal income taxation	58
Conclusion	65

TABLE OF AUTHORITIES

CASES: Page

Alexander v. "Americans United," Inc., 416 U.S. 752, 40 L.Ed.2d 518, 94 S.Ct. 2053 (1974)..... 39

Arkansas v. Texas, 346 U.S. 368, 98 L.Ed. 80, 74 S.Ct. 109 (1953).... 32

Bob Jones University v. Simon, 416 U.S.725, 40 L.Ed.2d 496, 94 S.Ct. 2038 (1974)..... 39

Brown v. Environmental Protection Agency, 521 F.2d 827 (9th Cir. 1975), vacated and remanded sub. nom. Environmental Protection Agency v. Brown, 431 U.S. 99, 52 L.Ed.2d 166, 97 S.Ct. 1635 (1977). 59

Brushaber v. Union Pacific Railroad, 240 U.S. 1, 60 L.Ed. 493, 36 S.Ct. 236 (1916)..... 63

Colorado v. Toll, 268 U.S. 228, 69 L.Ed. 927, 45 S.Ct. 505 (1925).... 38

District of Columbia v. Train, 521 F.2d 971 (D.C. Cir. 1975), vacated and remanded sub.nom Environmental Protection Agency v. Brown, 431 U.S. 99, 52 L.Ed.2d 166, 97 S.Ct. 1635 (1977)..... 59

Elrod v. Burns, 427 U.S. 347, 49 L.Ed.2d 547, 96 S.Ct. 2673 (1976)..... 55

CASES: (con't.) Page

Federal Energy Regulatory Commission v. Mississippi, ____ U.S. ____, 72 L.Ed2d. 532, 102 S.Ct. 2126 (1982)..... 53,56

Fry v. United States, 421 U.S. 542, 44 L.Ed.2d 363, 95 S.Ct. 1792 (1975)..... 46,47,53

Hodel v. Virginia Surface Mining & Reclamation Association, 452 U.S. 264, 69 L.Ed.2d 1, 101 S.Ct. 2352 (1981)..... 48,49,53 54

Illinois v. City of Milwaukee, 406 U.S. 91, 31 L.Ed.2d 712, 92 S.Ct. 1385 (1972)..... 39

Land v. Dollar, 330 U.S. 731, 91 L.Ed. 1209, 67 S.Ct. 1009 (1947)..... 37

Lane County v. Oregon, 74 U.S. (7 Wall.) 101 (1869)..... 45

Larson v. Domestic and Foreign Commerce Corp., 337 U.S. 682, 93 L.Ed. 1628, 69 S.Ct. 1457, reh.den., 338 U.S. 840, 94 L.Ed. 514, 70 S.Ct. 31 (1949)..... 37

Marbury v. Madison, 5 U.S. (1 Cranch) 60 (1803)..... 37

Maryland v. Environmental Protection Agency, 530 F.2d 215 (4th Cir. 1977), vacated and remanded sub.nom. Environmental Protection Agency v. Brown, 431 U.S. 99, 52 L.Ed.2d 166, 97 S.Ct. 1635 (1977)..... 58

CASES: (con't.) Page

Maryland v. Louisiana, 451 U.S. 725, 68 L.Ed.2d 576, 101 S.Ct. 2114 (1981)..... 43

Maryland v. Wirtz, 392 U.S. 183, 20 L.Ed.2d 1020, 88 S.Ct. 2017 (1973)..... 46

Massachusetts v. Mellon, 262 U.S. 447, 67 L.Ed. 1078, 43 S.Ct. 597 (1923)..... 34

McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316 (1819)..... 62

Missouri v. Holland, 252 U.S. 416, 64 L.Ed. 641, 40 S.Ct. 382 (1920)..... 33,37,38

National League of Cities v. Usery, 426 U.S. 833, 49 L.Ed.2d 245, 96 S.Ct. 2465 (1976)..... 31,33,45 46,47,48 50,51,53 56

Ohio v. Wyandotte Chemical Corp., 401 U.S. 493, 28 L.Ed.2d 256, 91 S.Ct. 1005 (1971)..... 42,43

Oklahoma ex rel. Johnson v. Cook, 304 U.S. 387, 82 L.Ed. 1416, 58 S.Ct. 954 (1938)..... 32

Oregon v. Mitchell, 400 U.S. 112, 27 L.Ed.2d 272, 91 S.Ct. 260 (1970)..... 37,42

Pollock v. Farmers' Loan & Trust Company, 157 U.S. 429, 39 L.Ed. 759, 15 S.Ct. 673, reh., 158 U.S. 601, 39 L.Ed. 1108, 15 S.Ct. 912 (1895)..... 44,50,60, 62,63

CASES: (con't.) Page

South Carolina v. Katzenbach, 383 U.S. 301, 15 L.Ed.2d 769, 86 S.Ct. 803 (1966)..... 37,42

Texas v. Florida, 306 U.S. 398, 83 L.Ed. 817, 59 S.Ct. 563 (1939)..... 35

United Transportation Union v. Long Island Railroad Co., 455 U.S. ____, 71 L.Ed.2d 547, 102 S.Ct. 1349 (1982)..... 51,52

Weston v. The City Council of Charleston, 27 U.S. (2 Pet.) 481 (1829)..... 31,50,59, 62

CONSTITUTIONAL PROVISIONS:

Article III, Section 2..... 27,35,38

Tenth Amendment..... passim

Sixteenth Amendment..... 62,63,64

STATUTORY PROVISIONS:

United States Code

26 § 7421(a)..... 39

26 § 7801..... 30

28 § 2201..... 39

Internal Revenue Code of 1954

§ 103..... 29,64

§ 7422..... 39

Statutes at Large	Page
Pub. L. No. 97-248, Tax Equity and Fiscal Responsibility Act of 1982, § 310(b)(1).....	passim
Pub. L. No. ____, Technical Corrections Act of 1982, § 306(b)(2).....	30
MISCELLANEOUS:	
45 Congressional Record 1696 (1910).....	63
Pension and Profitsharing Report Bulletin No. 16 (January 14, 1983) ¶ 233 at 41.....	30
Senate Report 97-494, Vol. 2, 97th Congress, 2d Session p. 242.....	54
p. 243.....	30
U. S. Code Congressional and Administrative News, No. 7 (September 1982) p. 217.....	54
p. 218.....	30
pp. 376-377.....	64
U. S. Code Congressional and Administrative News, No. 10 (December 1982), Cumulative Tables 98.....	29

JURISDICTION

The plaintiff State of South Carolina seeks to invoke the original jurisdiction of the Court pursuant to Article III, Section 2 of the United States Constitution which grants the Court original jurisdiction in an action between a State and a citizen of another State. The plaintiff State of South Carolina is a founding sovereign State of the United States and the defendant Donald T. Regan, who currently serves as the Secretary of the Treasury of the United States, is a resident and citizen of the State of Virginia.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Tenth Amendment to the United States Constitution provides:

> The powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people. U.S.CONST. amend. X.

Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 provides as follows:

> (b) OTHER OBLIGATIONS. --
>
> (1) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.-- Section 103 (relating to interest on certain governmental obligations) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:
>
> '(j) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.--
>
> '(1) IN GENERAL.-- Nothing in subsection (a) or in any other provision of law shall be construed to provide an exemption from Federal income tax for interest on any registration-required obligation unless the obligation is in registered form.
>
> '(2) REGISTRATION-REQUIRED OBLIGATION.-- The term "registration-required obligation" means any obligation other than an obligation which--
>
> '(A) is not of a type offered to the public,
>
> '(B) has a maturity (at issue) of not more than 1 year or
>
> '(C) is described in section 163(f)(2)(B).

'(3) SPECIAL RULES.--

'(A) BOOK ENTRIES PERMITTED.-- For purposes of paragraph (1), a book entry obligation shall be treated as in registered form if the right to the principal of, and stated interest on, such obligation may be transferred only through a book entry consistent with regulations prescribed by the Secretary.

'(B) NOMINEES.-- The secretary shall prescribe such regulations as may be necessary to carry out the purpose of paragraph (1) where there is a nominee or chain of nominees.' P.L. 97-248, 96 STAT. ____ (1982).

STATEMENT

On August 19, 1982, both houses of the United States Congress enacted Public Law 97-248, the "Tax Equity and Fiscal Responsibility Act of 1982" ("the Act"), and the President of the United States approved the Act on September 3, 1982. 1/ Section 310(b)(1) of the Act, which amends Section 103 of the Internal Revenue Code

---

1/ U.S. CODE CONG. & AD. NEWS, No. 10 (December 1982), Cumulative Tables 98.

of 1954 [I.R.C. §§ 1 et seq.], provides that any debt obligation which is required by that Section to be issued in registered form loses its exemption from federal income taxation if it is not so issued. Expressly intended to be included as a registration-required obligation is "any obligation of a State or local government, ... [2/] Although the registration requirements as well as the alternative sanctions imposed by Section 310(b)(1) were originally scheduled to apply to any obligation issued after December 31, 1982, later Congressional action suspended the effective date until July 1, 1983. [3/] The administration and enforcement of the provisions of Section 310(b)(1) is to be performed by or under the supervision of the defendant Secretary of the Treasury pursuant to 26 U.S.C. § 7801.

[2/] S.Rep. 97-494, Vol. 2, 97th Cong., 2d Sess. 243, reprinted in U.S.CODE CONG. & AD. NEWS, No. 7 (September 1982), Legislative History 218.

[3/] Technical Corrections Act of 1982 § 306(b)(2), reported in PENSION & PROFIT-SHARING REPORT BULLETIN No. 16 (January 14, 1983) ¶ 233 at 41.

SUMMARY OF ARGUMENT

This action puts in issue the constitutionality of Section 310(b)(1) of the Act, which the plaintiff contends is an unconstitutional attempt by the United States Congress to restrict the manner in which South Carolina may exercise its power to borrow money for public purposes through the issuance of State bonds. The plaintiff's position is supported by decisions of the Court, beginning with Weston v. The City Council of Charleston, 27 U.S. (2 Pet.) 481 (1829), that recognize the constitutional limitation placed on the power of the federal and State governments to tax the obligations of one another and by National League of Cities v. Usery, 426 U.S. 833 (1976), in which the Court held that the Congress may not "displace the States' freedom to structure integral operations in areas of traditional governmental functions." National League of Cities at 845-46.

ARGUMENT

I. The complaint manifests a justiciable controversy over which the Court has and should assume original jurisdiction.

A. The plaintiff State of South Carolina is the real party in interest.

While the Court's original jurisdiction expressly includes "Controversies ... between a State and Citizens of another State," the State must in fact be the real party in interest.

> In determining whether the interest being litigated is an appropriate one for the exercise of our original jurisdiction, we of course look behind and beyond the legal form in which the claim of the State is pressed. Oklahoma ex rel. Johnson v. Cook [304 U.S. 387]. Arkansas v. Texas, 346 U.S. 368 at 371 (1953).

That the plaintiff is the real party in interest herein cannot be disputed for its bonds are the ones which under Section 310(b)(1) of the Act must be issued in registered form or lose their tax-exempt status. In

asking the Court to preserve its sovereign right to issue bonds in bearer form (and to effect the savings available thereby) [4/] without risking unconstitutional sanctions, South Carolina seeks to protect its own interests. One interest arises from its affirmative duty as a sovereign to provide services essential to its citizens' health and welfare which it accomplishes by, inter alia, borrowing money to provide those services. A second interest arises from its affirmative right as a co-equal sovereign with the United States to reciprocal immunity from taxation. South Carolina asserts these interests in its capacity as a sovereign State, i.e., under the United States Constitution and the Tenth Amendment thereto. Missouri v. Holland, 252 U.S. 416 (1920); National League of Cities, et al v. Usery, 426 U.S. 833 (1976)

[4/] See, Complaint, Aff. ¶ 9, supra at 17-18.

(n. 7 at 836). 5/

The plaintiff's standing to sue also arises from the fact that it will be substantially damaged in monetary terms by the enforcement of Section 310(b)(1). Although the tax on registration-required obligations issued in bearer form will be paid by the bondholders, South Carolina as the issuer will in effect absorb the cost of the tax either by paying a greater rate of interest on its obligations or by registering those obligations at an increased cost to itself. 6/ If it chooses to do neither, its obligations will not be as salable as potential purchasers turn instead to the more financially attractive obligations of those States

---

5/ The Court's line of decisions holding that a State as parens patriae cannot sue to enjoin the enforcement of an allegedly unconstitutional act of Congress presents no obstacle to the assumption of original jurisdiction here because South Carolina does not assert a parens patriae interest. Cf., e.g., Massachusetts v. Mellon, 262 U.S. 447 (1923).

6/ See, Complaint, Aff. ¶ 8 and 9, supra at 16-18.

who do attempt to offset the effect of Section 310(b)(1).

B. The controversy is justiciable and is not barred by the sovereign immunity doctrine.

The case and controversy language of Article III, Section 2 of the United States Constitution, which has traditionally been interpreted to mean that courts are to restrict their adjudications to justiciable matters, necessarily applies to the exercise of the Court's original jurisdiction. Texas v. Florida, 306 U.S. 398 (1939).

South Carolina's Tenth Amendment claim seeks not an advisory opinion but instead the resolution of an immediate and concrete controversy. Section 310(b)(1) applies to all registration-required obligations issued after June 30, 1983, and, as its Treasurer states, South Carolina fully intends to issue general obligation bonds after June 30, 1983. 7/ The

---

7/ See, Complaint, Aff. ¶ 2, supra at 13.

mechanics of the issuance must begin well before that date, however, and the validity vel non of Section 310(b)(1) will determine in large part the amount of those bonds, their interest rate and their marketability. If South Carolina can know whether or not the provisions of Section 310(b)(1) are enforceable against its general obligations, it will be in an infinitely better position to make its fiscal decisions; for example, if Section 310(b)(1) cannot constitutionally be enforced against its obligations, then South Carolina will be able to issue those obligations at a substantial savings. 8/ But if Section 310(b)(1) is enforceable, then South Carolina must allow for the added costs of the issuance by, inter alia, adjusting its general appropriations in other areas. Regardless of the Court's decision on the merits, the impact of that decision will be certain and

---

8/ Id., ¶¶ 8 and 9, supra at 16-18.

significant. Again, South Carolina asserts that the controversy is real. 9/

Moreover, South Carolina's Tenth Amendment claim is not barred by the doctrine of sovereign immunity. The Court long ago declared that a suit to enjoin a federal officer from enforcing an allegedly unconstitutional statute does not constitute a suit against the sovereign, reasoning that "the conduct against which specific relief is sought is beyond the officer's power and is, therefore, not the conduct of the sovereign." Larson v. Domestic and Foreign Commerce Corp, 337 U.S. 682 at 690 (1949). See also, Oregon v. Mitchell, 400 U.S. 112 (1970); South Carolina v. Katzenbach, 383 U.S. 301 (1966); Land v. Dollar, 330 U.S. 731 (1947); Missouri v. Holland, 252 U.S. 416 (1920).

Finally, the Court has recognized that

9/ Nor does South Carolina's claim involve a nonjusticiable political question. See, e.g., Marbury v. Madison, 5 U.S. (1 Cranch) 60 (1803).

a bill in equity for injunctive and declarative relief is proper in this type of action. In Missouri v. Holland, supra, the Court upheld Missouri's right to bring a bill in equity to enjoin a federal official from enforcing allegedly unconstitutional regulations promulgated under the Migratory Bird Treaty Act. Although Missouri's Tenth Amendment claim was rejected, the Court declared that a bill in equity "is a reasonable and proper means to assert the alleged quasi-sovereign rights of a State." 252 U.S. at 431. See also, Colorado v. Toll, 268 U.S. 228 (1925).

C. The Court should assume original jurisdiction herein.

While the plaintiff recognizes that the language of Article III, Section 2 does not make the Court's original jurisdiction exclusive, Congress has effectively foreclosed

any lower court challenge herein. [10] There is therefore a compelling reason for the Court to assume original jurisdiction for otherwise the plaintiff will be without an available forum, adequate or otherwise, within which to assert its claim. Cf., Illinois v. City of Milwaukee, 406 U.S. 91 (1972).

The importance of promptly securing a definitive resolution to the fundamental constitutional issue is another compelling reason for the Court to hear this action originally. Because of the significant adverse

---

[10] The usual bases of judicial review of tax matters are available only to taxpayers. E.g., I.R.C. § 7422. Under the Anti-Injunction Act [26 U.S.C. § 7421(a)], no action may be maintained seeking to enjoin the levy or collection of federal taxes. This provision has been broadly construed and would no doubt emcompass the present situation. Cf., Bob Jones University v. Simon, 416 U.S. 725 (1974). Similarly, the Federal Declaratory Judgment Act [28 U.S.C. § 2201] expressly forbids declaratory judgments concerning tax matters and is generally held to be "at least as broad" as the Anti-Injunction Act. Alexander v. Americans United, Inc., 416 U.S. 752 at 759, n. 10 (1974).

impact which the provisions of Section 310(b)(1) will immediately have on the plaintiff's exercise of its governmental functions, it has a vital interest in having the question of the validity of Section 310(b)(1) resolved as expeditiously as possible. As hereinabove noted, South Carolina must make preparations to comply with Section 310(b)(1) if it is enforceable and those preparations involve outlays of money. If Section 310(b)(1) is not enforceable and these preparations need not have been made, South Carolina will have wasted that money. On the other hand, if Section 310(b)(1) is enforceable and South Carolina has not prepared to comply with its requirements, the marketability of its general obligation bonds will be seriously jeopardized. South Carolina cannot withstand without severe hardship the potential loss of money under either alternative. The fact that all fifty States will also be immediately economically burdened to a significant extent by the provisions of Section

310(b)(1) compounds the urgency of a definitive resolution. 11/

Moreover, the plaintiff's claim presents the precise issues on which the Court has declared its intent to concentrate the exercise of its original jurisdiction. In declining to assume original jurisdiction over a suit between a State and a citizen of another State which raised "no serious issues of federal law," the Court declared:

> ... This Court's paramount responsibilities to the national system lie almost without exception in the domain of federal law. As the impact on the social structure of federal common, statutory, and

---

11/ The requirements of Section 310(b)(1) apply to the issuance of obligations by all fifty States. The plaintiff alleges that it alone will be burdened by an extra $2.8 million on a single moderate sized sale of capital improvement general obligations. See, Complaint, Aff. ¶ 8, supra at 16-17. Even more staggering is the economic effect which Section 310(b)(1) will immediately have throughout the United States based on the total amount of general obligation bonds issued by other States in 1982 ($19.3 billion) and the total amount of municipal paper issued throughout the United States in 1982 ($74 billion). Id., ¶ 5, supra at 15.

> constitutional law has expanded, our attention has necessarily been drawn more and more to such matters.... Ohio v. Wyandotte Chemicals Corp., 401 U.S. 493 at 498 (1971).

Nothing involves serious issues of federal law more acutely than the proper relationship between the governments of the States and the United States in the federal system intended by the founding fathers. [12/] The Court is uniquely empowered to preserve the federal system by, inter alia, declaring and maintaining the provisions of the United States Constitution. Whether or not South Carolina can continue to function in its traditional role as a sovereign untrammeled by acts of the United States Congress raises a basic federal law issue, one which only the Court is able to resolve. See, e.g., Oregon v. Mitchell, 400 U.S. 112 (1971); South Carolina v. Katzenbach, 383 U.S. 301 (1966).

12/ The merits of the plaintiff's claim are argued more fully under Question II and Question III, infra.

Additionally, although the controversy is a crucial one and the issue is of great moment, the legal question is not complex. The dispute requires no discovery nor the taking of extensive testimony so that the Court will not become involved in the role of fact finder for which, it has stated, it is "ill-equipped." Ohio v. Wyandotte Chemical Corp., supra at 498.

In summary, this action is an appropriate one for the Court to exercise its original jurisdiction: the plaintiff is the proper party to raise the issues herein because Section 310(b)(1) injures it both monetarily and in its capacity as a sovereign State; the economic effect of the provisions of Section 310 (b)(1) is immediately substantial and far-reaching; and the issues raise serious and important concerns of federalism "fully in accord with the purposes and reach of [the Court's] original jurisdiction." Maryland v. Louisiana, 451 U.S. 725 at 744 (1981).

II. Section 310(b)(1) of the Act violates the United States Constitution and the Tenth Amendment thereto by abridging the plaintiff's power to borrow money.

South Carolina as a sovereign State possesses a long-recognized implied constitutional power to borrow money for public purposes. In Pollock v. Farmers' Loan & Trust Company, 157 U.S. 429 (1895), the Court declared:

> ... under the fundamental law, as to the power to borrow money, neither the United States on the one hand, nor the states on the other, can interfere with that power as possessed by each and an essential element of the sovereignty of each. 157 U.S. at 585.

The plaintiff's power to borrow money free from federal regulation arises, then, from its status as a sovereign power, which status is inherent in the federal system intended by the United States Constitution. See generally, Pollock v. Farmers' Loan & Trust Company,

supra; Lane County v. Oregon, 74 U.S. (7 Wall.) 101 at 104 (1869).

The borrowing power also expressly arises under the Tenth Amendment to the United States Constitution as a power "reserved to the States." In National League of Cities v. Usery, 426 U.S. 833 (1976), the landmark case on the Tenth Amendment, the Court considered the applicability of the minimum wage provisions of the Fair Labor Standards Act to the States and their political subdivisions. The cities and States challenged the United States Congress' authority to legislate minimum wage standards applicable to public sector employees, not as beyond its Commerce Clause power, but instead as prohibited by the Tenth Amendment, which imposes an affirmative limitation on that power. The Court overruled a previous decision and distinguished another, holding that "insofar as the challenged amendments operate to directly displace the States' freedom to structure integral operations in

areas of traditional governmental functions, they are not within the authority granted Congress...." 426 U.S. at 852. The decision overruled was Maryland v. Wirtz, 392 U.S. 183 (1973), which had upheld the extension of the Fair Labor Standards Act to State-operated schools and hospitals. Relying on Maryland v. Wirtz, the Court had later found that the Economic Stabilization Act, which provided for a wage freeze, could be properly applied to the States. Fry v. United States, 421 U.S. 542 (1975). The Court in National League of Cities declined to overrule Fry, even though it was based on Maryland v. Wirtz, but distinguished it in three particulars from National League.

First, Fry involved legislation which was aimed at an emergency situation and which was carefully limited in scope and time. In addition, the effect of the wage freeze was not to displace State choices but to require that the choices already in effect be maintained during the emergency. Finally, the Court in

National League of Cities noted that the statute in Fry actually reduced the pressures on State budgets rather than increased them. 426 U.S. at 853.

Like the legislation in National League of Cities, Section 310(b)(1) at issue here is distinguishable from the legislation in Fry. Just as the attempt to legislate wage provisions in National League of Cities impermissibly withdrew from the States the authority to make fundamental decisions, Section 310(b)(1) seeks to so economically restrict the alternatives available to South Carolina in the exercise of its power to borrow money that it has withdrawn from South Carolina any real freedom to issue obligations in the manner it deems most suitable to effect its responsibility to perform essential functions.

Since its decision in National League of Cities, the Court has clarified its position as to what requirements must be satisfied before a Tenth Amendment claim seeking to

invalidate Commerce Clause legislation can succeed. In Hodel v. Virginia Surface Mining & Reclamation Association, 452 U.S. 264 (1981), the Court interpreted National League of Cities to require:

> First, there must be a showing that the challenged statute regulates the 'States as States.' Second, the federal regulation must address matters that are indisputably 'attribute[s] of state sovereignty.' And, third, it must be apparent that the States' compliance with the federal law would directly impair their ability 'to structure integral operations in areas of traditional functions' [citations omitted]. 452 U.S. at 287-288.

The legislation at issue in Hodel was the Surface Mining Act which, in part, prescribed minimum performance standards that had to be met by individuals mining on certain types of land. The plaintiffs claimed that the States traditionally regulated land use and any attempt by the Congress to prescribe minimum standards violated the Tenth Amendment. The

plaintiffs' claim was unsuccessful because it failed to satisfy the first of the three requirements, i.e., that the challenged legislation regulated the States as States. The Court reasoned that the Surface Mining Act governed only the activities of private persons, that the States were not compelled to enforce the Act and that no State funds had to be expended because of the Act. 452 U.S. at 288.

The tax imposed by Section 310(b)(1) of the Act concededly falls initially on the holder of State general obligation bonds rather than on the State as issuer. Unlike the Mining Act provisions in Hodel, however, the effect of Section 310(b)(1) on State activities is not incidental. Under the Mining Act, the States were free to legislate their own programs within certain guidelines or to refrain from acting at all in which event the full regulatory burden would be borne by the federal government and imposed on individual

and corporate miners. It cannot be argued that under Section 310(b)(1) an issuing State is equally free to do nothing and that the burden will then fall only on the individual holder of its bonds. The Court has repeatedly recognized that a tax on the interest from government bonds burdens the issuer. See, Pollock v. Farmers Loan & Trust Company, supra; Weston v. City Council of Charleston, 27 U.S. (2 Pet.) 481 (1829).

The second requirement of the National League of Cities standard is that the challenged legislation must address matters that are indisputably attributes of State sovereignty, that is, the interest advanced by the State must involve "functions essential to separate and independent existence." 426 U.S. at 850. There can be no doubt that South Carolina's power to borrow money is a function essential to its separate and independent existence. Few "attributes of sovereignty" insure the independence

of a State more certainly than the power to raise money to remain financially secure. Every public service provided by South Carolina and its subdivisions is affected when its power to borrow money is interfered with. As in National League of Cities, where the Court noted that the legislation at issue withdrew from the States the authority to make those fundamental employment decisions upon which their systems for the performance of their essential functions rested [426 U.S. at 851], the power to borrow money is likewise an attribute of sovereignty upon which South Carolina's entire system for the performance of its integral State functions rests.

The third and final requirement of National League of Cities is that compliance with the legislation will seriously impair the State's ability to structure its integral operations. This third requirement was fatal to the Tenth Amendment claim of State railroad employees in United Transportation Union v. Long Island Railroad Company, 455 U.S. ____,

102 S.Ct. 1349 (1982). The Court in United Transportation found that the operation of a railroad by the State was not an integral part of its government activity but was a function traditionally performed by private industry. Federal regulation of such railroads under the Commerce Clause was held not to impair a State's ability to function as a State. 102 S.Ct. at 1354. It cannot be seriously contended that the borrowing of money is a "function previously performed by the private sector" such that application of the Tenth Amendment would allow the State's assumption of this function to erode the federal government's authority to regulate in an area traditionally allowed it. As discussed earlier, nothing is so fundamental to the States' ability to perform their essential functions than the ability to raise money to support their operations. Because it seriously interferes with South Carolina's power to raise money, Section 310(b)(1) impermissibly impairs South

Carolina's ability "to fulfill its role in the Union." 102 S.Ct. at 1356.

One final consideration in analyzing National League of Cities is the Court's declaration that in some cases the nature of the federal interest advanced may require State submission even though all of the above discussed requirements are met. Hodel, 452 U.S. at 288, n. 29. This "overriding interest" factor has been characterized as an exception to National League of Cities [13/] and, although the Court has considered no cases involving this exception since it was first enunciated, the emergency situation in Fry was cited as an example of circumstances that would justify requiring a State to submit to federal encroachment on its sovereignty. Id. The plaintiff would urge the Court to refrain from engaging in

---

13/ See, Federal Energy Regulatory Commission v. Mississippi, ____ U.S. ____, 102 S.Ct. 2126 at 2147, n. 4 (1982) (Justice O'Connor, concurring in part and dissenting in part).

the balancing action suggested in the footnote in Hodel except where the essential nature of the State function being overridden is in doubt. There can be no such doubt with respect to South Carolina's power to borrow money, long recognized by the Court as essential to its sovereignty as a State. Moreover, there is no overriding federal interest advanced by the enactment of Section 310(b)(1) which would even remotely justify the resulting blow to South Carolina's sovereignty.

Having made this assertion, South Carolina is not unmindful of the reasons asserted by the Senate Finance Committee for the change sought to be effected by Section 310(b)(1). [14/] However justified they may be and however salutary the result intended to be

---

[14/] S.REP. 97-494, Vol. 2, 97th Cong. 2d Sess. 242, reprinted in U.S. CODE CONG. & AD. NEWS, No. 7 (September 1982) 217. The Senate Finance Committee's action, however, was not unanimous. Id., Minority Views of Senators Long, Bentsen, Matsunaga, Moynihan, Boren and Mitchell 376-377.

reached by the enactment of Section 310(b)(1), the invasion of South Carolina's sovereign right and power is a far greater evil than that sought to be cured. If the United States Congress can require that South Carolina's obligations must be issued in registered form in order to keep intact its immunity from federal income taxation, then federal legislation similarly limiting the time of issuance, amount, maturity date, interest rate, market and purpose of those obligations would also be possible. In other words, the Congress could provide that in the year 1983 South Carolina can issue only $5 million of its general obligation bonds which must be sold only in July, 1983, must mature in 1988, must bear 5 per cent interest, must be expended for highway purposes only and must be sold only to citizens of South Carolina. If unhalted by the Court, the Congress could thus reduce South Carolina's once-called sovereign power to borrow money to a matter of congressional grace or whim.

In his dissent in Elrod v. Burns,

427 U.S. 347 (1976), Chief Justice Burger characterized National League of Cities as follows:

> Only last ... we took steps to arrest the downgrading of States to a role comparable to the departments of France, governed entirely out of the national capital. Constant inroads on the powers of the States to manage their own affairs cannot fail to complicate our system and centralize more power in Washington. 427 U.S. at 375-376.

The exigencies of economic change have whittled away some of the limitations that were formerly thought to exist, principally through the judicial expansion of "general welfare" powers. Each time such action occurs, the federal system is undermined. As Justice Powell observed in his dissent in Federal Energy Regulatory Commission, supra, quoting a constitutional law professor on the danger of such gradual encroachment by the federal sovereign:

> 'Of course, no one expects Congress to obliterate the states, at least in one fell

> swoop. If there is any danger, it lies in the tyranny of small decisions--in the prospect that Congress will nibble away at state sovereignty, bit by bit, until someday essentially nothing is left but a gutted shell.' 102 S.Ct. at 21 (quoting L. Tribe, American Constitutional Law 302 (1978)).

The United States Constitution was written with the express guarantee, i.e., the Tenth Amendment, that the States are to retain all the attributes of sovereignty in certain areas. The power to borrow money is without question one power that is "reserved to the States." However arguably inconsiderable the effect may be, Section 310(b)(1) represents an attempt by the United States Congress to retard the ability of South Carolina to function as a sovereign in an area reserved to it by the United States Constitution and, to that extent, violates the United States Constitution and in particular the Tenth Amendment thereto.

III. Section 310(b)(1) of the Act violates the United States Constitution by subjecting the interest paid on the debt obligations issued by the plaintiff in bearer form to federal income taxation.

In providing that the interest paid on State obligations which are not in registered form is not exempt from federal income taxation, Section 310(b)(1) of the Act goes beyond the power of the United States Congress -- the interest on such obligations is protected from taxation by the United States Constitution.

Furthermore, this protection from taxation exists irrespective of the power of the Congress to impose registration requirements. "[I]t is one thing ... to decide that a state which chooses to engage in activities which Congress has a right to control must do so on Congress' terms ... but it is quite another to extract from a state a most fundamental aspect of its sovereignty." Maryland v. EPA, 530 F.2d 215 at 225-226 (4th Cir. 1977),

vacated and remanded sub.nom. EPA v. Brown, 431 U.S. 99 (1977); District of Columbia v. Train, 521 F.2d 971 at 990-994 (D.C. Cir. 1975), vacated and remanded sub.nom. EPA v. Brown, 431 U.S. 99 (1977); Brown v. EPA, 521 F.2d 827 at 837-842 (9th Cir. 1975), vacated and remanded, 431 U.S. 99 (1977).

That interest on State obligations may not be taxed by the federal government has long been established. In Weston v. The City Council of Charleston, 27 U.S. (2 Pet.) 481 (1829), Chief Justice Marshall, speaking for a majority of the Court, held that the ordinance of the City of Charleston imposing a tax of "twenty-five cents upon every hundred dollars of ... six and seven per cent stock of the United States" was unconstitutional. Counsel for the taxpayer argued:

> The contract of the general government is invaded, and its credit impaired. Its competency to negotiate loans may be destroyed by the admission of this power of taxation. There are two sources of revenue which are essentially the right of the general government -- that of imposing duties, and that of borrowing money on the credit of the

> nation. The safety of the whole depends upon the free and undisturbed exercise of these powers. 27 U.S. (2 Pet.) at 482.

Chief Justice Marshall agreed:

> If the right to impose the tax exists, it is a right which in its nature acknowledges no limits. It may be carried to any extent within the jurisdiction of the State or corporation which imposes it, which the will of each State and corporation may prescribe. 27 U.S. (2 Pet.) at 487.

In Pollock v. Farmers' Loan & Trust Company, 157 U.S. 429 (1895), the Court considered, among other questions, whether the income from State-issued securities could be taxed to the holder under the Revenue Act of 1894. Recognizing that previous case law forbade federal taxation of the property or revenues of a State, Chief Justice Fuller concluded:

> But we think the same want of power to tax the property or revenues from the states or

> their instrumentalities exists in relation to a tax on the income from their securities, and for the same reason, and that reason is given by Chief Justice Marshall in Weston v. Charleston, ..., where he said: 'The right to tax the contract to any extent, when made, must operate on the power to borrow before it is exercised, and have a sensible influence on the contract. The extent of this influence depends on the will of a distinct government. To any extent, however inconsiderable, it is a burden on the operations of government. It may be carried to an extent which shall arrest them entirely. * * * The tax on government stock is thought by this court to be a tax on the contract, a tax on the power to borrow money on the credit of the United States, and consequently to be repugnant to the Constitution.' Applying this language to these municipal securities, it is obvious that taxation on the interest therefrom would operate on the power to borrow before it is exercised, and would have a sensible influence on the contract, and that the tax in question is a tax on the power of the states and their instrumentalities to borrow money, and consequently repugnant to the Constitution. 157 U.S. at 585.

This doctrine of intergovernmental immunity had its genesis in Chief Justice

Marshall's decision in McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316 (1819). Weston v. City Council, supra, applied the doctrine to taxes levied by the State upon securities of the federal government and the Pollock decision recognized that the converse was true by extending that immunity to the interest paid on State and municipal bonds. 15/

The ultimate result of Pollock was to invalidate the Revenue Act of 1894 because it unconstitutionally failed to apportion the income tax among the several States. In response to this result, the Congress passed the Sixteenth Amendment to the United States Constitution in 1913. But the debate in the

---

15/ After the decision was rendered, Pollock was reargued and new opinions were filed at 158 U.S. 602 (1895). The rehearing allowed the Court to "broaden the field of inquiry" and to determine to which of the two classes of taxes, direct or indirect, the income from rents of real estate and from bonds belonged. The holding that taxation of the receipts from municipal bonds is a tax on the power to borrow money and, consequently, repugnant to the United States Constitution remained unchanged. 158 U.S. at 618.

United States Senate makes it clear that the Sixteenth Amendment was not intended to give to the Congress the power to tax the income from State obligations. It was conceded that such a power would destroy the federal system. See, 45 CONG. REC. 1696 (1910).

Just two years after the adoption of the Sixteenth Amendment, in Brushaber v. Union Pacific Railroad, 240 U.S. 1 (1916), the claim was made that the effect of the Sixteenth Amendment was to extend the class of subjects which could be constitutionally taxed by the Congress because of the inclusion of the phrase "incomes, from whatever source derived." After reviewing the history of the Sixteenth Amendment and its relation to the Pollock decision, the Court reached the conclusion that the Sixteenth Amendment did not expand the federal taxing power to new subjects.

> It is clear on the face of [the Amendment] that it does not purport to confer power to levy income taxes in a general sense, -- an authority already possessed

> and never questioned, -- or to limit and distinguish between one kind of income taxes and another, but that the whole purpose of the Amendment was to relieve all income taxes when imposed from apportionment from a consideration of the source whence the income was derived. 240 U.S. at 17-18.

This pronouncement of the law has rested without serious challenge from 1916 to 1982. From the date of the adoption of the Sixteenth Amendment to the present the Congress has made no effort to tax the interest paid by the States to the holders of their bonds. The provisions of Section 103 of the Internal Revenue Code do not create the tax exemption that applies to the interest paid by the States upon their bonds; instead, they are necessarily purely declarative of the existing state of the law.

Through oblique means the Congress is now seeking to avoid the decisions of this Court and thus to amend the United States Constitution by legislative fiat. South Carolina

urges the Court to let stand the long accepted interpretation of the Constitution itself, to continue to recognize the federal system and to continue to uphold the essential corollary that State governmental action is free from congressional interference except as otherwise provided in the Constitution itself. The provisions of Section 310(b)(1) which conditionally tax the interest paid on State obligations are patently unconstitutional and South Carolina cannot without doing violence to the United States Constitution be forced to accept those provisions as an unconstitutional alternative.

CONCLUSION

This legislation is constitutionally infirm for two reasons. It asserts congressional controls in a field preserved to the States, thus impermissibly intruding on the sovereignty of the States, and, in blind-side fashion, it unconstitutionally asserts the right of the federal government to tax the

interest paid by States on their debt obligations despite clear and sound precedent to the contrary.

The constitutional powers of the States must not be carelessly abrogated. The continued existence of the federal system secures the liberties of the citizens of the United States as no other form of government could and far outweighs any remote administrative convenience attaching to the plan here promoted by the United States Congress. That plan must be judicially voided.

Respectfully submitted,

T. TRAVIS MEDLOCK
Attorney General

C. TOLBERT GOOLSBY, JR.
Chief Deputy Attorney General

DAVID C. ECKSTROM
Assistant Attorney General

GRADY L. PATTERSON, III
Assistant Attorney General

Post Office Box 11549
Columbia, SC 29211
(803) 758-3970

SINKLER GIBBS & SIMONS
Huger Sinkler
Karen LeCraft Henderson*
Faye A. Flowers

Post Office Box 11458
Columbia, SC 29211
(803) 765-1885

ATTORNEYS for Plaintiff.

*Counsel of Record.

February 7th, 1983

CERTIFICATE OF SERVICE

I, KAREN LeCRAFT HENDERSON, counsel of record for the plaintiff and a member of the Bar of the Court, do hereby certify that, in accordance with Rule 28.4(a), three (3) copies of the Motion for Leave to File Complaint, Complaint and Supporting Brief were served on all parties required to be served on this date by depositing same in the United States mail, first-class postage prepaid, and addressed as follows: The Solicitor General of the United States, Department of Justice, Washington, D.C. 20530 and The Honorable Donald T. Regan, Secretary of the United States Treasury, Department of the Treasury, 1500 Pennsylvania Avenue, N.W., Washington, D.C. 20220.

This 7th day of February, 1983.

Karen LeCraft Henderson
KAREN LeCRAFT HENDERSON

Post Office Box 11458
Columbia, SC 29211